REGULATION NO. 14

WHEREAS, Section 5-2A-8 of the Alabama Banking Code provides that the Superintendent of Banks may, with the concurrence of a majority of the members of the State Banking Board, promulgate reasonable rules and regulations;

AND WHEREAS, The Superintendent of Banks, with the concurrence of a majority of the members of the State Banking Board, recognizes the need and desirability for rules and regulations pertaining to maximum legal lending limits allowable under Section 5-5A-22 of the Alabama Banking Code,

NOW THEREFORE, be it known that the Superintendent, with the concurrence of the State Banking Board, does hereby promulgate the following regulation.

Section 5-5A-22 of the Alabama Banking Code prohibits banks from making loans to any one borrower which, when combined with all other loans to such borrower, would cause total loans to that borrower to exceed:

- Ten percent of the capital accounts of the bank, if such loans are unsecured, or
- Twenty percent of the capital accounts of the bank if loans in excess of 10 percent of capital are fully secured.

Section 5-5A-22 further requires that all loans exceeding 10 percent of the capital accounts of the bank be approved by the bank's board of directors, a committee of the board of directors, or a loan committee. Such approval must be recorded in the minutes of the board or committee. If such loans are approved by a committee, the committee must have at least three (3) members to be considered valid for this purpose. Whenever a loan officer, committee member, or committee learns that a loan or loans have been made in excess of the Section 5-5A-22 limits, the officer, committee member, or committee must report the violation to the full board at the next regularly scheduled board meeting. Upon the Superintendent learning through an examination that loans have been made in excess of the Section 5-5A-22 limits, he may require the bank to adopt such approval practices as he deems necessary to prevent future violations of the limits. Such approval practices might include, but not be limited to, advance approval of all loans over ten percent of the bank's capital and reporting of borrowers' total debt when such loans are brought to the board or committee for approval. Failure of the bank to implement such required approval practices will be deemed a violation of this regulation.

This regulation must be applied in conjunction with (not in place of) the provisions of Section 5-5A-22.

1) The total capital base for lending limits contained in §5-5A-22 of the Alabama Banking Code includes: capital stock, surplus, undivided profits, subordinated capital notes or debentures, and the allowance for loan and lease losses. Reserves for contingencies that are not set aside to cover any specific expected losses may also be included. Specific contingency reserves and unrealized gains or losses on debt securities available for sale are not to be included.

2) The capital base for computing the maximum lending limit shall be the amounts shown for capital stock, surplus, undivided profits, subordinated capital notes or debentures, and the allowance for loan and lease losses reflected on the bank's most recent quarterly Report of Condition (Call Report). Specific contingency reserves and unrealized gains or losses on debt securities available for sale are not to be included.

3) For legal lending limit purposes, the definition of a loan shall be the same as the definition of an extension of credit contained in §215.3 of Federal Reserve Board Regulation O. This definition includes, but is not limited to:

a) An advance by means of an overdraft, cash item, or otherwise,

b) Issuance of a standby letter of credit (or other similar arrangement regardless of name or description),

c) Granting (by an executed note or written, loan agreement) of a line of credit, draw note, or other commitment on the part of a bank to extend credit,

d) Making of a direct loan or acceptance of paper sold under a guaranty, repurchase agreement, or other recourse arrangement,

e) Making or renewal of any loan, line of credit, or extension of credit.

4) The amount of the loan for the purpose of legal lending limits shall be the principal balance of the loan (or the total amount of a line of credit, draw note, or other commitment) including any fees and charges added to the principal balance of the loan, but shall not include interest collected and not earned that is added to the loan or interest accrued and not collected that is not added to the loan. Interest capitalized by adding back to the note or by any other means upon renewal or extension of the note shall be included.

For a line of credit, draw note, or other commitment on the part of the bank to extend credit, the total amount of such line including the maximum amount drawn and available to be drawn shall be included.

5) The purpose of statutory loan limits is to prevent one borrower or a relatively small and economically related group from borrowing an unduly large portion of the bank's funds. In order to have diversification by spreading loans out among a relatively large number of creditworthy borrowers who are not economically related, all direct or indirect loans to borrowers, their partnerships, firms, limited liability companies, or corporations must be aggregated and regarded as single loans. The procedures to be used in determining which loans to aggregate shall include the following:

a) Direct or indirect loans to a borrower's spouse will be aggregated and treated as one loan to the borrower unless the lender can prove to the satisfaction of the Superintendent that each spouse has a separate net worth and such net worth of each is not dependent on decisions made or actions taken by the other.

b) Loans made to or for the tangible economic benefit of a borrower and the borrower's associates or controlled companies which are substantially dependent upon the same source for repayment or which were made for the same ultimate purpose will be aggregated and treated as one loan for legal lending limit purposes.

i) Associates means members of a partnership or unincorporated group of individuals or companies allied to own or control business ventures or entities.

ii) Controlled company means one which a borrower directly or indirectly through immediate family members or associates effectively manages or controls.

c) If a borrower owns 35% or more of a corporation or limited liability company by stock ownership or otherwise, the direct or indirect loans to this company and to the borrower would be treated as one loan to the borrower.

d) If a borrower owns less than 35% of a corporation or limited liability company, the direct and indirect loans to the company and to the borrower will be aggregated and treated as one loan to the borrower to the extent that the borrower guarantees or is otherwise legally liable for the loans to the company.

e) If a borrower owns less than 35% of a corporation or limited liability company but in the opinion of the Superintendent effectively manages the company and the borrower's presence or managerial ability are vitally necessary for the continued successful operation of the company, then direct or indirect loans to the company would be aggregated with direct or indirect loans to the borrower.

f) If a borrower is a general partner, the direct and indirect loans to the partnership and to the general partner will be aggregated and treated as one loan to the general partner.

g) If a borrower is a limited partner, the direct and indirect loans to the partnership and to the limited partner will be aggregated and treated as one loan to the limited partner to the extent that the limited partner guarantees or is otherwise legally liable for the loans to the partnership.

h) When in the opinion of the Superintendent an individual or company appears to be fully responsible for the debt service on paper that is purported to be "without recourse" through the practice of paying off such seriously delinquent paper or other indications of responsibility, then the amount of such paper will be aggregated and treated as one loan to the individual or company.

6) If any loan or aggregate of loans exceeds ten per cent (10%) of the total capital base, such excess must be fully secured by good collateral or other ample security. All subsequent loans shall likewise be fully secured by good collateral or other ample security. A maximum of twenty per cent (20%) of the total capital base may be loaned to one individual or borrower where all in excess of ten per cent (10%) is fully secured as defined above.

A loan may be purported to be secured but, for lending limit purposes, may, in the opinion of the Superintendent, be considered unsecured. Such a case could come about where the stated collateral is so poor as to have little value, where the lien on the collateral is not perfected within a reasonable time, or where a combination of factors including, but not limited to, missing documentation of the bank's lien position, amount of collateral, location of collateral, or condition of collateral casts substantial doubt on the collateral's existence or value. In such cases, the Superintendent shall provide the bank a period of time, determined by the Superintendent, to correct the documentation deficiencies, prove the value of collateral, obtain additional collateral, or otherwise correct the violation before imposing the penalties prescribed by §5-5A-22.

7) There are certain instances when loans to any one borrower may exceed 20% of the total capital base. Exceptions provided for in this regulation are in addition to the exceptions specified in §5-5A-22(c)(1)-(4). The exceptions detailed here are granted pursuant to §5-5A-22(c)(5) that lists as exceptions "such other loans, liabilities or transactions as shall from time to time be established by regulations of the state banking department." Such exceptions are primarily dependent of the loans' collateral and the controls over that collateral. There would be such a large number of different types of collateral that it would be impossible to list them all. The following requirements, however, have to be met for any such loan to conform to this section:

a) The collateral must be cash or equivalent to cash or have a readily established market value and be a product for which there is a ready sale in the open market. There must be no question regarding the market value. If the condition or grade of the collateral is questionable, it will not be acceptable as collateral in this instance.

b) The collateral must be assigned to the bank in such a manner that in the event of default the bank can take possession and title at its discretion. Also, the collateral must be in possession of or under absolute control of the bank at all times.

c) In the event that the market value of the collateral declines, additional collateral must be

provided immediately or the loan reduced appropriately so that, at all times, the loans are fully secured with the market value of collateral at least equal to the amount of the loan.

d) Such loans must be approved in advance by the bank's board of directors, a committee of the board of directors, or a loan committee. Such approval must be recorded in the minutes of the board or committee.

Management of the bank is responsible for providing the secured and unsecured lending limits to the board of directors (and/or committee responsible for approving loans over ten percent of capital). At a minimum, the limits should be reported to the board or committee quarterly at the first meeting following the due date for submission of the bank's call report. A notation of the lending limits should be entered in the minutes of the board or committee meeting at which they are reported or otherwise documented in a manner satisfactory to the Superintendent. Management is also responsible for informing all lending personnel affected by the lending limits.

Management's responsibility to inform the board and lending personnel does not, however, relieve directors and lending officers of their duty to ascertain the limits prior to approving or making loans.

This regulation shall be effective October 1, 1998.

s/Wayne C. Curtis
Superintendent of Banks